

February 21, 2002

This letter responds to your correspondence with the Indiana Department of Financial Institutions (the "Department") regarding the Automatic Overdraft Protection Program (the "Program"). We have had an opportunity to review your materials and have discussed the issues with the staff of the Department.

The Comptroller of the Currency ("OCC")'s Interpretive Letter #914 sets forth the minimum guidelines that must be followed for the Program to pass muster under federal laws and regulations. However, assuming that the Program addresses the federal concerns, there are issues that arise under state law. This letter sets forth the position of the Department regarding the Program.

The effect of the Program is to increase the fee income of the bank by encouraging customers to intentionally write non-sufficient funds ("NSF") checks. Although the program may be valuable to customers who might inadvertently or infrequently write an NSF check, banks participating in the program will, in essence, attempt to entice their customers to write NSF checks more frequently resulting in greater fee income. The Department finds this to be contrary to both public policy and generally accepted safety and soundness practices. NSF fees should be utilized to discourage consumers from writing bad checks. Such fees are meant to foster responsible banking practices by customers. The proposed program seems to accomplish the exact opposite. An NSF fee should be punitive in nature and serve as a deterrent to the writing insufficient fund checks. If a bank feels compelled to increase fees because of the soaring costs and expenses involved in handling insufficient fund checks, then it has the option of raising its NSF fees.

In addition to this general public policy issue, there is a matter of graver importance under Indiana law. A program such as that being proposed arguably entices a customer to unwittingly commit a criminal offense. Under IC 35-43-5-5, it is a Class A misdemeanor when a person knowingly or intentionally issues or delivers a check knowing there are insufficient funds in the bank. Since the Program gives no assurance of coverage in the event of an overdraft, but leaves that to the discretion of the bank, a customer will never be certain that a bad check will be covered. This could make both the customer and the bank accountable under the criminal statute.

On the other hand, if a customer can rely on the bank to cover their checks, then there is an agreement between the two parties, making the Program nothing more than a line of credit. As such, it is subject to Indiana's Uniform Consumer Credit Code ("UCCC") and its fees and interest rate limits. The rates or fees contained in the Program greatly exceeds those limits and would be deemed refundable violations if in excess of 36% APR. If in excess of 72% APR, then such rates would be considered a felony and any line of credit with interest would be void. Even though the documents to be provided to customers regarding the Program repeatedly point out that this service is a "non-contractual courtesy" and the bank is "not obligated to pay any item presented for payment", the Department would look beyond these statements to the actual operation of the plan, a matter of examining the substance of the agreement rather than the form.

It is a reasonable conclusion that the Program is either a loan (overdraft privilege), between the bank and the customer subject to the parameters of the UCCC, or it is not a loan. If the Program is not a typical overdraft arrangement then the arrangement could result in a criminal offense.

No assurances can be given at this point regarding how the Department will consider the proposed Program. However, please be assured that if the Program is found to not be an extension of credit, the Department will take whatever steps necessary to make a bank cease and desist from participating in a transaction that could be considered a criminal offense. There are apparently differences in implementation/underwriting at the various participating

institutions. The Department examiners will review the program when we conduct either a compliance examination or a safety and soundness examination. Independent decisions will be made by the examiners as to how the overdrafts and related loans will (or will not) be classified.

Sincerely,

J. Philip Goddard
Deputy Director and General Counsel

cc: Charles Phillips, Director
James Cooper, Deputy Director
Mark Tarpey, Consumer Credit Supervisor